Qualified Charitable Distributions: How to Have Your Cake and Eat It Too

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If you know the sweet taste of being one of nearly half of all US households to make regular charitable contributions, then the icing on that cake may well be that it is possible to do good for yourself while doing well for others! If you are at least 70.5 years old and have an Individual Retirement Account (IRA), then consider a Qualified Charitable Distribution (QCD).

Qualified Charitable Distributions allow individuals to withdraw money from IRAs on a federal income tax-free basis. Here's how this tax-free charitable donation works:

1. Possess an IRA (Note this does not include 401(k) plans, active SEP IRAs, nor active SIMPLE IRAs)
2. Attain age 70.5 (Note this does not coincide with the RMD age of 73)
3. Choose qualified charity(ies) to receive the donation(s)
4. Donate **directly** from the IRA to the qualified charity
5. Inform your tax preparer of the Qualified Charitable Distribution(s)

While there is no limit on the number of charities to which you can donate, you are limited to an annual QCD amount of $100,000 per person. The pièce de résistance of QCDs is that if you are in Required Minimum Distribution (RMD) status and make a QCD, your RMD and the resulting taxable income will be reduced by the amount of your charitable donation.

For example, assume your IRA RMD in 2023 is $50,000. You choose to directly donate $20,000 to your local church from your IRA and consume the remaining $30,000 on personal spending. Your taxable income from IRA withdrawals would only be $30,000. Utilizing QCDs is an effective strategy for reducing taxable income—particularly in situations when you already intend to donate money to charity from a different source of funds. While your taxable income is reduced with a QCD, you do not also receive an itemized charitable deduction. However, a reduction in your tax base will generally be more advantageous than an itemized tax deduction.

The introduction of the Secure Act 2.0 earlier this year delivered a couple of slight changes to QCD policy. Beginning in 2024, the maximum annual QCD limit of $100,000 will become indexed to inflation, increasing marginally each year. A bigger cake! Additionally, starting in 2023, the law now allows a one-time opportunity to use a QCD to fund $50,000 into a split interest entity, namely: Charitable Remainder Unit Trust (CRUT), Charitable Remainder Annuity Trust (CRAT), or Charitable Gift Annuity (CGA). The entity must be solely funded by the $50,000 QCD, so you can't use a CRUT or CRAT you've already established. Unfortunately, that could result in added expense for a limited benefit, but it still may be a worthwhile course of action for some individuals.